

OUR 27TH YEAR

Roy Hardaker on why conservative investors should load up on US-dollar investments. Page 4.

Stephen Gadsden on exercising caution when markets exhibit premature exuberance. Page 6.

Visit our Website: adviceforinvestors.com

FLASH ADVICE

- ◆ RioCan REIT: Hold/Buy, Page 3.
- ◆ GGOF Monthly High Income Fund: Hold, Page 4.
- ◆ Bank of Montreal 5.95% Series 10 preferred: Buy, Page 5.
- ◆ Burlington Resources: Hold/Buy, Page 7.
- ◆ Royal Bank: Hold/Buy, Page 7.
- ◆ Berkshire Hathaway Class B: Hold/Buy, Page 8.

May 2003/Second Report ◆ Single Copy: \$10.00

Volume 27, Issue No. 10

THE MONEY LETTER[®]

STRATEGIES FOR SUCCESSFUL INVESTING

TRENDS

◆ **INCOME TRUST GUIDANCE.** Ever since Standard & Poor's took over the Canadian Bond Rating Service, the US-based giant has been adding a variety of features of special interest to Canadian investors.

One of the most useful initiatives is the coverage they're providing on the burgeoning field of income trusts. S&P Canada has taken the lead in developing a ratings system for these popular securities, similar to that used for bonds and preferred shares.

They're called Stability Ratings, and they are designed to reflect the relative stability of the cash distribution of a specific fund, and the outlook for the future based on current information. The grading system goes from SR-1 (best) to SR-7 (worst). An income fund with an SR-1 rating is deemed to have "the highest level of expected sustainability and the lowest level of expected variability in a fund's distribution stream relative to other rated Canadian income funds." In other words, the distributions are judged to be both safe and dependable. **RioCan REIT** (see my update on Page 3) gets a very good SR-2 rating, with a Stable outlook.

Continued on Page Two

MARKET STRATEGY

Yield makes a comeback

INCOME BUILDER

Gordon Pape

IT HAD TO HAPPEN. EVERY IDOL has feet of clay, at least in the eyes of the media. The latest target is financial guru Warren Buffett, one of the richest people in America and an icon to investors everywhere.

According to some critics, the Grand Old Man of Money has lost his touch. His **Berkshire Hathaway Inc.** empire has become an unwieldy



Contributing Editor Gordon Pape is a successful investor and the well-known author of many books on personal investing. He or his family may hold securities mentioned in his column.

conglomerate composed of dozens of disparate entities, which are collectively beyond the management capabilities of even the most astute CEO. It is doomed to collapse in upon itself, or so the story goes.

Perhaps. But unless and until that happens, my inclination is to take all this nay-saying with a big grain of salt. For several decades, Mr. Buffett has proven repeatedly that his unlikely blend of business acumen and down-home folksiness produces sound investment decisions most of the time.

Continued on Page Two

Gordon Pape, from Page One

Remember back in the late '90s when he was dismissed as out of touch when he refused to invest in high-tech companies because he didn't understand them? How wise that decision now looks with the

benefit of hindsight.

Even though the insurance segment of his business continues to have problems, the company just reported an 89% jump in first-quarter net earnings, to US\$1.73 billion, or US\$1,127 per class A share. If Berkshire Hathaway is on the verge

of imploding, it certainly isn't evident in the numbers.

So, like many of my fellow contributors at *The MoneyLetter*, I continue to pay close attention to what Mr. Buffett has to say about the state of the investment world. And he offered some insightful if rather deflating comments during the company's May 3 annual meeting, held as usual in Omaha, Nebraska. (See also Dr. Michael Graham's report on Page 8.)

I was particularly struck by the outlook for the stock markets in the next few years that was offered by Mr. Buffett and his long-time friend and associate, Charles Munger (referred to simply as "Charlie" in the company's annual reports).

Their view is that a return to double-digit stock gains is unlikely in the foreseeable future. Mr. Buffett told some 12,000 shareholders that equity profits will probably average somewhere between 6% and 7% annually, including dividends. His reasoning is simple: Current stock prices still aren't cheap, and don't offer anything like the values we saw back in the mid-'70s or early '80s, when deep recessions gutted the markets.

The comments made this month reinforced the caution expressed in the company's 2002 annual report, which was released in February. At the time, here's what Mr. Buffett wrote:

"Despite three years of falling prices, which have significantly improved the attractiveness of common stocks, we still find very few that even mildly interest us. That dismal fact is testimony to the insanity of valuations reached during The Great Bubble. Unfortunately, the hangover may prove to be proportional to the binge."

As a result, his company would

TRENDS, from Page One

Unfortunately, only a relatively small percentage of the income funds sold in Canada are rated — only 29 as of this writing. That's because a company must pay for a rating, and until the S&P cachet becomes as important for income trust investors as bond ratings have been for years, many income funds won't bother. Also, a fund that is likely to get a low rating may prefer to remain anonymous. The lowest-rated funds right now are energy funds, pegged at SR-5, which are known for the volatility of their distributions.

The ratings aren't the only help available to income investors from S&P Canada. You can also read a number of reports on income securities, including a very detailed analysis of real estate investment trusts.

There is no charge to the public for any of this information, but you must register on the S&P Website to gain access to it. Go to www2.standardandpoors.com and click on "Canada" in the "Choose Region" box. Then click on the "Complete Guide to Stability Ratings" box on the right.

◆ **INTEREST RATE REVERSAL?** Bank of Canada Governor David Dodge keeps warning about more interest rate increases to come because of the need to contain inflation in this country. Forgive me if I'm skeptical.

The rapid rise of the Canadian dollar has put a great deal of pressure on Canadian manufacturers and threatens to damage our export-based economy. One of the main contributing factors to the loonie's surge is the large interest-rate spread between Canada and the US.

Additional hikes in Canada's rate structure would only exacerbate the situation and could result in a US75¢ loonie within a few months. The problem would be compounded if the US Federal Reserve Board lowers American rates again. Indeed, with the Fed clearly nervous about the possibility of deflation, its bias right now is towards further easing from the already low 1.25% rate.

It's hard to imagine inflation gaining strength in Canada while the US trends towards deflation. Moreover, the drop in energy prices that followed the end of the Iraq war should ease inflationary pressures considerably in the coming months.

Taking everything into account, a hold-the-line policy on Canadian rates now appears more likely over the summer than more increases. It's even possible we could see Mr. Dodge reverse course and implement a quarter-point cut.

This would be good news for bond investors, who profited handsomely during the bear market. For the past couple of years, many experts have been saying that the good times for bonds were over. They have yet to be proven correct.

◆ **NEW TV SHOW.** You might want to catch my new television program, called *Real Life Money*, which will debut on the Global Television Network and its affiliated stations during the weekend of June 21. Along with a panel of experts, we'll be helping people who are in financial difficulty find solutions to their problems. Check your local listings for times in your area.

— Gordon Pape

“sit on the sidelines,” he said. “With short-term money returning less than 1% after tax, sitting it out is no fun. But occasionally successful investing requires inactivity.”

A glance at the first-quarter balance sheet shows that Mr. Buffett has been practicing what he preaches. Berkshire Hathaway’s equity assets dropped by almost \$1 billion from Dec. 31 to March 31. In the meantime, cash balances rose to \$16.1 billion from \$10.3 billion.

All this should raise some basic questions: Why invest in stocks at all at this stage, if one of the world’s greatest financial minds is sitting it out? And if you do invest, what goals should you have, and what kind of returns should you expect?

It comes down to this: Are you investing in the stock market for income or for capital gains?

Traditionally, we have thought of equities in terms of their capital gains potential and looked to other types of securities for income. But it may be time — indeed, past time — to revisit that approach.

If Mr. Buffett is correct (and, of course, there are many who disagree with him), then the capital gains potential for stocks generally is very limited for the next few years. Of course, there will be exceptions and we at *The MoneyLetter* will continue to search them out. But if his projections turn out to be right, once dividends are taken out of the equation, we could be looking at average capital gains returns in the 5% range for several years. That’s not nearly adequate for the market risk involved.

This means we need to refocus on the income-generating potential of equities and equity-like securities. The Bush Administration is aggressively trying to do just that with its controversial plan to remove all personal taxation of dividends paid by

US companies. No similar initiative has been discussed here, but the existing Dividend Tax Credit already provides an incentive for investors.

Adding to the importance of refocusing on income are several recent studies that show that dividend-paying stocks stood up better during the bear market and tend to outperform non-dividend stocks over the long term. So by opting for dividends, you may also be enhancing the capital gains potential of the securities in your portfolio.

In evaluating dividend-paying stocks or other income securities, here are some key points to look for:

➤ **Financial strength.** Corporations or trusts cannot make distributions from profits they don’t earn. Occasionally, they may do so for a period of time in order to maintain investor confidence (**Noranda Inc.** is a current example), but it can’t go on indefinitely.

➤ **Consistency.** Take a close look at the organization’s dividend history. See how long it has been paying distributions, and look especially closely to see whether the payments have ever been reduced.

➤ **Steady increases.** An organization with a history of steady dividend increases is especially attractive.

One of the best examples in Canada of a company that has a long track record of dividend increases is **Enbridge Inc.** (TSX: ENB; recent \$46.70), a recommendation of my colleague Roy Hardaker.

Back in 1996, the annual dividend on the common stock was \$1.015 (adjusted for subsequent splits). In that year, the shares traded in a range from \$15.88 to \$21. If you bought at the highest price point of the year, your dividend yield at the time would have been 4.8%.

Each year since, Enbridge has

increased its dividend. In 2003, the company is on track to pay out \$1.66 a share. If you had bought at \$21 in 1996 and had held your shares ever since, your yield today, based on the original price, would be 7.9%. That’s a very attractive return on a blue-chip utility stock. As a bonus, you would be sitting on a fat capital gain, with the shares recently trading in the \$46 range. Who said that dividend-paying stocks were dull?

➤ **My advice:** If you purchased shares on the basis of Roy Hardaker’s original recommendation, keep holding them. If you don’t own them, buy now. The current dividend yield is 3.6%.

Here’s an update on two of my recommendations that meet the criteria for top-notch income securities.

HOLD/BUY

◆ **RIOCAN REIT** (TSX: REI.UN; recent \$13.59; originally recommended as Counsel Real Estate Investment Trust March ’94/Second Report at \$6.04*; last mentioned July ’02/Second Report as a hold at \$12.95; adjusted for 2-for-1 split). RioCan released its first-quarter results this month, posting continued solid performance. Rental revenue was up 24% year-over-year to just under \$121 million. Net earnings increased by 8%, to \$42.5 million (27¢ per unit) compared with \$39.5 million (27¢ per unit) for the comparable period in 2002.

Like Enbridge, RioCan has a history of modest but steady distribution increases since 1995. That year, unitholders received 57.5¢ per share (split-adjusted). In 2003, the trust is expected to pay out \$1.14 per unit,

Continued on Page Four

**The average daily closing price for the week after The MoneyLetter was mailed.*

Gordon Pape, from Page Three

almost exactly double the 1995 distribution. Based on the recent price of \$13.59, the shares are currently yielding 8.4%.

There's not much capital gains potential here, but the income stream is very dependable, and a significant portion of the distribution is received on a tax-deferred basis if the units are held outside a registered plan. **My advice:** Hold existing positions. If you're an income-oriented investor and you don't own units in this top-quality real estate trust, buy.

HOLD

◆ **GGOF MONTHLY HIGH INCOME FUND CLASSIC UNITS** (recent \$9.55; originally recommended November '96/Second Report at \$9.73; last mentioned July '02/Second Report as a hold/buy at \$9.61). This fund is now closed to new investors, but existing unitholders may maintain their positions. I suggest you do so.

The unit price has slipped slightly since my last review, but the units continue to generate good cash flow, some of which is tax-advantaged. Payments are holding steady at 6¢ per unit per month, or 72¢ a year. That's a cash-on-cash yield of 7.5% based on the recent price of \$9.55. The fund invests in a wide range of income trusts, with RioCan as its single largest position. **My advice:** Hold.

Following the closure of this fund, the company announced a replacement, **GGOF Monthly High Income II Fund**, with a slightly different mandate. So far, it has outperformed the original version, so it's worth a look. However, I want to see a little more history before I formally recommend it. ▼

CONSERVATIVE INVESTOR

A strengthening loonie calls for a more

GREENBACK PORTFOLIO

Roy Hardaker

THE EVENTS OF THE PAST FEW months have indeed been full of "shock and awe." A war in Iraq followed by a quick victory, an outbreak (and subsequent containment) of a particularly nasty virus here and in Asia, and now increasing fear of the mosquito-borne West Nile virus.

Economically, the severe decline in the value of the US dollar relative to the world's leading currencies is causing major concern about international trade balances and their effect on individual trading nations.

Our Canadian dollar has risen to its highest level against the US dollar in more than five years, trading recently at US73¢. Many pundits are predicting that the loonie will climb as high as US74¢ by the end of 2003.

The effect of the loonie's rise from a record low of US61.75¢ in January 2001 is currently being felt by our major export industries whose profits are starting to plunge. Export businesses have enjoyed fat returns

for the past couple of years and have been coasting on the need to control costs, productivity, and currency rates.

But importers, benefiting from a higher exchange rate, may not be able to pass on the savings from their lower costs, which would traditionally be inflationary. This time, despite a favorable exchange rate, a slowing economy will cut into importers' profits — not exactly stimulative to the economy, but at least it's non-inflationary.

These forces, combined with a still-sluggish economy in the US, have affected the most volatile and important statistic, unemployment. This has jumped sharply, to 6.0% in the US and to 7.5% in Canada. But home sales are still strong, and optimistic analysts believe these will decline only slightly.

Meanwhile, the Bank of Canada raised its key overnight lending rate (the rate at which major participants in the money market borrow and lend one-day funds to each other) in both March and April, in an effort to bring inflation back to its target of 2% from a recent reading of 4.5% in the consumer price index. The posture of the Bank of Canada now



Contributing Editor Roy W. Hardaker, MBA, FCSI, is vice-president of a major investment dealer. With 40 years' experience in the bond and stock markets, he specializes in conservative portfolio management. His clients own securities mentioned in his column.

appears to be have changed from aggressive action to one of neutrality with careful monitoring — the result of a slowdown in economic growth.

Our Bank Rate (the minimum rate at which the Bank of Canada extends short-term advances to banks) currently stands at 3.50% compared with the 0.75% Federal Funds rate in the US. The US Federal Reserve Board has not changed rates since its unexpected cut of half a percentage point last November. Unlike the Bank of Canada, which has been targeting inflation, the Fed appears to be focusing on the possibility of deflation (what it calls an “unwelcome substantial fall in inflation”). As a consequence, further rate cuts may well be coming. The problem is that lower rates will not stimulate the US economy.

US DOLLAR

For decades, the US has not cared about borrowing vast sums to support its extravagant buying of external goods and services. Because of its colossal size, the capital markets raised the funds to pay for these huge trade deficits. Perhaps a cheap US dollar is what the US needs to stimulate its economy.

The US does not worry about its trading partners, only about what is beneficial to its economy. So if interest rates are low, there is no incentive for foreign capital to invest in the US dollar. But where else can it go for liquidity, variety, and a huge banking system? Many things will happen if the US dollar stays weak for a long period, but the main thing to remember is this: The US will survive on its own terms, not the rest of the world's.

As a consequence, I believe the stage is set in the US for lower rates of interest, low inflation (perhaps

deflation), a slowing economy, and a continued weak dollar.

What are the implications for conservative investors? Do we continue with a policy of seeking reasonable income from investments that provide safety of capital?

I believe conservative investors should look at their US dollar position. For several years, I've been recommending that you allocate 25% of your portfolio to US dollar-denominated securities. With the current exchange rate around US73¢ after a rapid runup, I recommend you take cash balances to a total of 10% of your portfolio and purchase US dollar investments.

Canadian issue, US dollar-denominated preferred shares are scarce, but I've unearthed one for you. Fortunately, there is a more reasonable supply of US-pay bonds. Here are my recommendations:

BUY

◆ **BANK OF MONTREAL 5.95%, SERIES 10 US-PAY PREFERRED** (TSX: BMO.PR.V; recent \$27.90, to yield 5.3%; \$25 par; redeemable Feb. 25, 2012, at \$25). 🟢 *My advice:* Buy.

◆ **CANADA MORTGAGE AND HOUSING CORP. 2.95%, DUE JUNE 2, 2008** (recent \$101.41, to yield 2.65%). 🟢 *My advice:* Buy.

◆ **PROVINCE OF ONTARIO 4.375%, DUE FEB. 15, 2013** (recent \$104.60, to yield 3.80%). 🟢 *My advice:* Buy.

There are three key advantages to these securities: no withholding tax; Canadian tax credits on the preferred shares; and no US tax interference.

If the Canadian dollar rises to around US75¢, then eliminate non-US foreign holdings and use the proceeds to boost US dollar positions

by another 10% of the portfolio. If the Canadian dollar then strengthens from that level, a further 5% can be transferred to US dollar assets.

You may ask, “What about all these great foreign equity funds, stocks, and so on?” My response is that the US still drives the global economy and will continue to do so. Like it or not, we are an appendage of the US economy, and we should act accordingly.

CANADIAN DOLLAR

For the domestic portion of your defensive portfolio, here are some Canadian-dollar-denominated income-oriented investments that will meet our criteria for income and safety. First, let's look at some preferreds:

BUY

◆ **CIBC 6% NONCUMULATIVE SERIES 24 PREFERRED** (TSX: CM.PR.B; recent \$26.14, to yield 5.7%; \$25 par; redeemable Jan. 31, 2011, at \$25; S&P-rated P1-low; originally recommended February '02/First Report at \$25.79*). 🟢 *My advice:* Hold/buy.

◆ **MARITIME LIFE 6.1% NONCUMULATIVE SERIES 3 PREFERRED** (TSX: MMF.PR.C; recent \$26.30, to yield 5.8%; \$25 par; redeemable Dec. 31, 2007, at \$26; S&P-rated P1-low). 🟢 *My advice:* Buy.

◆ **POWER FINANCIAL CORP. 6% NONCUMULATIVE SERIES I PREFERRED** (TSX: PWF.PR.I; recent \$26.56, to yield 5.6%; \$25 par; redeemable April 10, 2008, at \$26; S&P-rated P1-low). 🟢 *My advice:* Buy.

Remember the gross-up and cred-

Continued on Page Six

**The average daily closing price for the week after The MoneyLetter was mailed.*

it system for tax purposes that applies to dividends from Canadian corporations. A dollar in dividends nets a top bracket Ontario taxpayer 68.67¢ after tax. To produce the same net amount from interest, you need to receive a gross amount of about \$1.28. This means that a dividend yield of 6% produces the same net after tax as a 7.69% interest yield.

High-quality bonds, of course, should be a mainstay of any conservative investment portfolio, and I've recommended many over the years. Here are three that are currently attractive.

BUY

◆ **CANADA MORTGAGE AND HOUSING CORP. 5%, DUE JUNE 1, 2004** (recent \$101.70, to yield 3.33%; rated AAA).

◆ **CANADA MORTGAGE BANK 4.4%, DUE MARCH 15, 2008** (recent \$100.89, to yield 4.19%; rated AAA).

◆ **FARM CREDIT CORP. 5%, DUE SEPT. 10, 2004** (recent \$99.70 to yield 3.26%; rated AAA).

Because bond quotes and availability vary from day to day and from broker to broker, I recommend you check with your financial adviser for up-to-date information on any of these issues.

Remember, too, that bond purchases generally are made in minimum retail amounts of \$50,000 and up, so that your broker can give you the best "spread" — the difference between the rate at which your broker buys the bond and the rate at which he or she offers it to you. Generally, the higher the dollar amount for investment, the smaller the spread charged. ▼

OUTLOOK

I hate to rain on anyone's parade, but some pundits have a case of

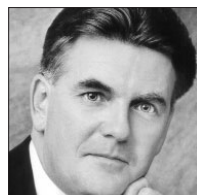
PREMATURE EXUBERANCE

Stephen Gadsden

WITH MAJOR MARKET INDEXES IN the black for the first time this year, assorted talking heads at such founts of investment wisdom as CNBC and ROBTv are falling all over themselves to declare that the worst of the bear is past and that it's time to plunge into stocks again. But before you go whole hog into stocks, consider the following:

• **Unemployment.** Recent unemployment figures show a rising tide in both Canada (7.5%) and the US (6%), but neither accounts for the tens of thousands of people who have stopped looking for work. It gets worse. A recent survey by US firm Challenger, Gray & Christmas showed that layoff announcements rose an unheard of 71% in April alone. And the US Conference Board reported that its Help-wanted Index fell to its lowest level since 1964.

Cue: *Consumers who fear for their jobs cut or eliminate spending.*



Contributing Editor Stephen Gadsden is an author, columnist, and media commentator on investing and money management. He is the author of 12 books on personal finance, including *The Canadian Mutual Fund Handbook* and *Retire Rich!* and a practicing Certified Financial Planner. He or his family may hold securities mentioned in his column.

This is a disaster for an economy in which 67% of annual GDP arises from consumer spending.

• **Inventories of manufactured goods.** Inventories of US manufactured goods have declined substantially. This is often seen as a positive sign for economic recovery. But the widely used "just-in-time" production and supply format has weakened this indicator's reliability. Low inventory now tends to be deflationary because only enough goods are produced to satisfy immediate needs, which provides no pricing power to manufacturers. Canadian manufacturers are also feeling the pinch of a deflating American economy as the demand for US-bound exports begins to drop.

Cue: *Falling demand for goods coupled with just-in-time production means lower manufacturing demand, less capital spending, and more unemployment — a triple whammy for stock markets.*

• **Weakening US dollar.** Between May 1995 and the end of 2002, the US dollar appreciated 47%. To date, the greenback has contracted a mere 9%. Some noted economists assert the American dollar has to decline another 30% to

40% before it will spark increased domestic production and exports to any significant degree. As a consequence, Canada's trade with the US will drop off severely, causing misery for Canada's commodities and manufacturing sectors.

Cue: *Cost-conscious US consumers turn to less expensive goods and services, which reduces demand for higher-priced Canadian imports. Lower demand inevitably translates into lower manufacturing, lower profits, and increasing unemployment for Canadians.*

➤ **Canada's trade deficit.**

Because 85% of Canada's exports depend on American consumers and the welfare of the US economy, an invigorated Canadian dollar will make Canadian goods and services less attractive to the huge US marketplace. No matter how good our products and services, price is the biggest determinant of sales. As Canadians realize the increased purchasing power of a strong domestic currency, they will purchase foreign goods at the expense of their own. The result, of course, will be an increasing foreign trade deficit and a lower standard of living at home.

Cue: *A negative trade deficit means more domestic capital is leaving the country than is staying. This situation hits domestic production hard and lowers GDP. The long-term consequences of weak productivity are higher interest rates demanded by foreign investors, weak capital markets, and a lower standard of living.*

➤ **Corporate profitability.** I have catalogued the projected earnings of a dozen or so blue-chip US companies over the past two years. What I've seen isn't reassuring. The trend has been for companies to methodically lower investor expectations of

corporate profitability with each passing quarter. At the time of writing, this process has occurred eight quarters in a row and has reached such desperate levels that even remotely positive news is perceived by equity markets as an indication of better times ahead. Unfortunately, future corporate profitability continues to rely more on cost-cutting and massaging of corporate earnings through pro forma reporting than on increasing revenues.

Cue: *If you lower your profit expectations far enough, you're bound to meet them. If you exclude accounting items that depress your future earnings, it's also easy to present an attractive picture of corporate health. The problem is you're deluding yourself and your shareholders into believing your financial situation is better than it is. This nonsense began in mid-2001 and continues to this day.*

➤ **Questionable valuations.**

Price/earnings ratios for the Dow Jones Industrial Average, the S&P 500 Composite Index, and the Nasdaq Composite Index are still well above their respective historical averages of 8:1, 15:1, and 18:1. Share prices of some individual companies are attractive on their own, of course, but the prospects for overall long-term corporate growth are decidedly uncertain.

Cue: *Just because a company's share price is attractive compared with its future earning power, it doesn't mean you can ignore the economy. The economy is the consequence of a healthy GDP, which is dependent on a free-spending consumer.*

➤ **Government and consumer debt.** US public debt amounted to \$6.4 trillion as of May 5, 2003. The Bush administration's anticipated

budget deficit for 2003 is an additional \$304 billion. Other economists think that the government shortfall will be closer to a whopping \$425 billion. The US national savings rate has deteriorated to -1.8% for the first time in decades and is expected to plummet further as the economy weakens.

Cue: *As with any individual budget, debt draws off capital that might otherwise be used for investment and spending. With US federal, individual, and state debt increasing every day, the likelihood of a strong capital market rebound is remote.*

The best advice I can give you is to continue to focus on securities of top-notch companies like the ones I've recommended, in particular, those in the following sectors:

HOLD/BUY

◆ **BURLINGTON RESOURCES INC.** (NYSE: BR; recent US\$51.06; originally recommended April '02/Second Report at US\$40.81*). Energy.

◆ **EDWARDS LIFESCIENCES CORP.** (NYSE: EW; recent US\$30.65; originally recommended June '02/First Report at US\$23.51*). Health sciences.

◆ **LOBLAW COS. LTD.** (TSX: L; recent \$59.35; originally recommended January '03/Second Report at \$52.60*). Food distribution.

◆ **ROYAL BANK OF CANADA** (TSX: RY; recent \$60; originally recommended September '02/Second Report at \$53*). Banking.

◆ **WASTE MANAGEMENT INC.** (NYSE: WMI; recent US\$24.59; originally recommended December '02/Second Report at US\$23.76*). Pollution control. ▼

**The average daily closing price for the week after The MoneyLetter was mailed.*

REPORT FROM OMAHA

TRUST! AT A TIME WHEN THIS most basic investment ingredient has never been more lacking, it has never been more needed. More than anything else, this is what drew 12,000 fans from far and wide to Omaha, Nebraska on the first weekend in May, for the 38th annual general meeting of **Berkshire Hathaway Inc.**

These days, not many chief executives are accorded a standing ovation at their annual general meetings. Granted, Berkshire had a very good 2002, the 10% growth in its per-share book value comparing with a negative 22% in the S&P 500 Composite Index. In short, Berkshire had outperformed the broad stock markets by a whopping 32%.

Nevertheless, this aside, it was the folksy, worldly-wise opinions of Warren Buffett (chairman and chief executive officer) and Charlie Munger (vice-chairman) — the one age 72, the other 78 — that everyone had come to hear. Messrs. Buffett and Munger exude trust and integrity — this time more than ever in the customary 5½-hour Q&A dialogue with their audience.

We were reminded that investing is a straightforward process of discipline, patience, and understanding. In reaffirming their “old-fashioned” approach (“It’s hard to teach new dogs old tricks”), they waxed strongly (to loud applause) on the need to grow rich “with your shareholders, not off your shareholders.”

A question about current stock market levels brought the reasoned reply that an annual return of 7% to 8%, made up of growth in line with gross domestic product (about 3%), an add-on for inflation (about 2% to 3%), and a running dividend yield (about 2%), “probably isn’t bad.” But only provided there is no comparison with the great bubble and the “insane” valuations — and returns — of the 1990s.

Another interesting reflection was that the way to own stocks without fretting is to focus on the value you judge them to offer, rather than their day-to-day price in stock markets that are there “to serve you, not to instruct you.” Because “you will be right if your facts and reasoning are correct.” Not day-by-day, but over time, as Berkshire Hathaway’s 22% average annual growth in per-share book value since inception amply testifies.

In the same value context, Buffett and Munger welcome price declines as a way to add more cheaply to one’s portfolio.

A year ago I returned from Omaha reinforced in my belief that these two companies fitted the Berkshire mold of excellence and value. They still do: **Power Corporation of Canada** (TSX: POW; recent \$41.17) and **Thomson Corporation** (TSX: TOC; recent \$41). **My advice:** Buy more.

This time, I would add most, if not all, of the other names in my Top Dozen list (see “Canada’s Strengths,” in our March ’03/Second Report). On this list I feel especially good about the following energy companies, in light of what was said about the future for energy, a field Berkshire is getting into in a big way through 80%-owned Mid American Energy Holdings (“You’re talking big money, not lemonade stands.”): **EnCana Corp.** (TSX: ECA; recent \$47.76); **Husky Energy Inc.** (TSX: HSE; recent \$16.60); **Suncor Energy Inc.** (TSX: SU; recent \$24.23). **My advice:** Buy more.

Last, but not least, of course, Warren Buffett and Charlie Munger, still sharp and active, could be around for a good many years yet. I hope so, not only because they are so refreshingly unique, but also because there is nothing in the world like an investment in Berkshire Hathaway — anywhere! A year ago, I recommended the **Berkshire Hathaway Inc. Class B shares** (NYSE: BRK.B; recent US\$2,452; originally recommended May ’02/Second Report at US\$2,513.60*). **My advice:** Buy more! — **Dr. Michael Graham**

* The average daily closing price for the week after The MoneyLetter was mailed.

THE MONEYLETTER®

STRATEGIES FOR SUCCESSFUL INVESTING

Vol. 27, No. 10

May 2003/Second Report

Contributing Editors: Richard Croft, Stephen Gadsden, Michael R. Graham, Ph.D., Roy W. Hardaker, Jon J. Kanitz, Ph.D., Eric Kirzner, David Louis, J.D., Gordon Pape

*The MoneyLetter** is published twice a month by MPL Communications Inc. Contents copyright © 2003 by MPL Communications Inc. All rights reserved. Reproduction in whole or in part without permission is prohibited. Brief extracts may be made with due acknowledgment. Information presented herein is not guaranteed.

Opinions expressed are not necessarily those of the publishers. Management and shareholders of MPL Communications Inc., editors, and contributors may at times have positions in mentioned securities.

Subscription Rate: \$127.00 per year. Single copies: \$10.00 each. Quantity rates on application.

Moving? Please let *The MoneyLetter* Reader Services know three weeks in advance. Send your new address, with postal code, and the effective date. If possible, enclose the address label from a recent issue.

Letters: Letters to the Editor will be considered for publication. We regret we cannot provide personal investment or tax counselling.

Subscription, account, and customer service:

Outside Toronto call toll-free:

1-800-804-8846

Toronto: 416-869-1177

Fax: 416-869-0456

E-mail: customers@mplcomm.com

Website: www.adviceforinvestors.com

MPL Communications Inc.

133 Richmond Street West
Toronto, Ontario M5H 3M8

**The MoneyLetter* is a Registered Canadian Trade Mark of MPL Communications Inc.

Publications Mail Registration Number 10652

Return Postage Guaranteed

GST Number R121844328

We acknowledge the financial assistance of the Government of Canada, through the Publications Assistance Program (PAP), toward our mailing costs.

From time to time we make our subscription list available to companies and organizations whose products and services we believe may be of interest to you. If you do not want your name to be made available, please check here and return with your mailing label.

ISSN 0703-7613

Printed in Canada